

BEFORE THE STATE BOARD OF EQUALIZATION  
OF THE STATE OF CALIFORNIA

In the Matter of the Appeal of )  
GEORGE S. AND MABLE L. DUKE )

Appearances:

For Appellants: Morris Michelson  
Public Accountant

For Respondent: Gary Paul Kane  
Tax Counsel

O P I N I O N

This appeal is made pursuant to section 18594 of the Revenue and Taxation Code from the action of the Franchise Tax Board on the protests of George S. and Mable L. Duke against proposed assessments of additional personal income tax in the amounts of \$564.21 and \$281.12 for the years 1961 and 1962, respectively.

During the years on appeal George S. Duke (hereafter referred to as "appellant") was engaged in the trucking and logging businesses and also in subdividing real estate. In his books and records he used the cash receipts and disbursements method of accounting.

Appellant's real estate subdivision activities included the purchase of land and the holding of that land for ultimate sale to customers. In 1961 and 1962 such purchases of real property by appellant totalled \$16,836.44 and \$6,840.19, respectively. He made no sales of land in 1961, and in 1962 such sales amounted to \$909.00. All of the real property acquired in those years was sold in 1966.

Appellant and his wife filed joint California personal income tax returns for 1961 and 1962. In each of those returns they deducted as business expenses the cost of the real estate which appellant had purchased during the year. Respondent disallowed those deductions on the ground that the amounts disbursed by appellant to acquire real estate were capital expenditures which could only be deducted in the year when the land was sold. Respondent's disallowance of those claimed expense deductions gave rise to this appeal.

Appellant contends that a real estate dealer should be allowed to deduct the cost of land as a currently deductible business expense under section 17202 of the Revenue and Taxation Code. We cannot agree.

It is a fundamental principle of income tax law that amounts paid to acquire land or to improve it represent capital expenditures rather than ordinary and necessary business expenses,, (4A Mertens, Law of Federal Income Taxation, § 25.25.) As was stated by the Board of Tax Appeals in the case of R.E. Thompson, 7 B.T.A. 391, rev'd on other grounds, 28 F.2d 247,

That the amount paid for such an item [i.e., land] was a capital expenditure and therefore not deductible from gross income, either on the receipts and disbursements or the accrual basis, is too well established to admit of questioning. (7 B.T.A. 391, 396.)

Generally the cost of property represents its basis (Rev. & Tax. Code, § 18042), which is subtracted from the amount received on a later sale or exchange of that property, in order to determine gain or loss on the transaction, (Rev. & Tax. Code, § 18031.) In this regard there is no statutory provision allowing different treatment where the purchaser of real property is a dealer in real estate. We must conclude, therefore, that appellant was not entitled to deduct the cost of real property as a business expense in the year of purchase.

Appellant further contends that a real estate dealer receives discriminatory treatment as compared to sellers of other goods and merchandise because he is not allowed to use the inventory method in determining the cost of goods sold in any particular year. The same Contention was unsuccessfully made by a real estate dealer in Atlantic Coast Realty Co., 11 B.T.A. 416,

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In view of the above facts and authorities we must sustain respondent's action in this matter.


## ORDER

Pursuant to the views expressed in the opinion of the board on file in this proceeding, and good cause appearing therefor,

IT IS HEREBY ORDERED, ADJUDGED AND DECREED, pursuant to section 18595 of the Revenue and Taxation Code, that the action of the Franchise Tax Board on the protests of George S. and Mable L. Duke against proposed assessments of additional personal income tax in the amounts of \$564.21 and \$281.12 for the years 1961 and 1962, respectively, be and the same is hereby sustained.

Done at Sacramento, California, this 6th day  
of November , 1967, by the State Board of Equalization.

Paul R. Leake, Chairman  
John W. Lippich, Member  
Kent R. Lippich, Member  
\_\_\_\_\_, Member

ATTEST: , Secretary